

Schedule of Audit Findings and Responses

State of Washington Military Department

1. The Military Department has an incorrect interpretation of state regulations regarding counting, reconciliation and certification of its asset inventory.

Background

In fiscal year 2009, the Department reported owning equipment valued at approximately \$9.8 million, consisting primarily of technology items such as communications equipment, laptops and personal computers.

The Office of Financial Management (OFM) provides state agencies with a set of required, minimum standards to be used to control and account for public assets. The required standards are documented in the *State Administrative and Accounting Manual*. The Department included most of these requirements in its own policies and procedures.

For fiscal year 2008, we reported concerns regarding the Department's tracking and valuation of assets, physical inventory and reconciliation process, and training provided to staff responsible for these activities. The Department developed a corrective action plan to address those weaknesses and in August 2009 reported to OFM the issues had been resolved.

Description of Condition

We reviewed the Department's plan and performed tests to verify if the corrective actions had been instituted. We found the Department still has not completed a full physical inventory of assets nor has it reconciled discrepancies for sections within the Department that did conduct an inventory.

Cause of Condition

In our prior audit, we informed the Department that its policies and procedures, if followed, were sufficient to perform a proper inventory. However, management instead implemented a new process which is not sufficient. That process is based on an inaccurate interpretation of state requirements. Management did provide guidance to staff; however it did not address all inventory requirements.

Effect of Condition

In addition to prior weaknesses still existing, we identified additional concerns. The Department's lack of sufficient instruction to employees resulted in employees using different counting methods and documentation that was inconsistent and insufficient to show what assets had actually been counted. Department management stated it only counted assets over two years old. It conducted only a sporadic count of assets less than two years old.

Without proper direction and oversight of the inventory process, employees are unaware of all requirements to conduct and reconcile inventory. Therefore, Department assets are at higher risk of loss or misappropriation without detection.

Recommendation

We recommend the Department consult with OFM to ensure it understands the requirements for asset tracking and reconciliation, the risks associated with noncompliance and to ensure its own policies and procedures adequately address those risks. We further recommend the Department complete its inventory counts of all assets, reconcile any differences, remove any missing or surplus assets from its inventory and certify the completed inventory.

Department's Response

The Department is neutral with the finding that we have an incorrect interpretation of state regulations regarding counting, reconciliation and certification of its asset inventory. We look forward to the opportunity to demonstrate to OFM that we do understand the requirements for asset tracking and reconciliation, the risks associated with noncompliance and to ensure that our new policy and procedures adequately address those risks. We have held up the final approval of our new policy due to the finding in this audit, however as of this writing we have completed the inventory counts of all assets within the period of this audit (through June 30, 2009), reconciled any differences and removed any missing or surplus assets from our inventory. Once we get confirmation from OFM that our new policy and procedures adequately address the regulations regarding counting, reconciling and certification of our asset inventory, we will certify the completed inventory

Auditor's Remarks

We appreciate the cooperation and assistance provided by the Department throughout the audit. We will follow up with the Department to review the status of its corrective action at a later date.

Applicable Laws and Regulations

RCW 43.19.1917, Records of equipment owned by state – Inspection, states:

All state agencies, including educational institutions, shall maintain a perpetual record of ownership of state owned equipment, which shall be available for the inspection and check of those officers who are charged by law with the responsibility for auditing the records and accounts of the state organizations owning the equipment, or to such other special investigators and others as the governor may direct.

State Administrative and Accounting Manual (SAAM) 30.45.10, Physical Inventory Frequency, states in part:

Conduct physical inventories at least once every other fiscal year for all inventorable assets except as noted below.

Due to the stationary nature of certain assets (such as land, infrastructure, buildings, improvements other than buildings, and leasehold improvements), performing a physical inventory every other fiscal year is not required.

State Administrative and Accounting Manual (SAAM) 20.15.30.c, states in part:

Agency management at all levels is responsible for internal control under their span of control. Management should make it clear that **agency staff** have explicit or implicit control activity duties including: delivery of services to the public; producing information for the management control system; maintaining financial information; and inspecting or maintaining physical assets. Management is also responsible to convey the importance of internal controls to all personnel both by what they say and what they do. If management is willing to override controls, then the message that controls are not important will be conveyed to employees.

State Administrative and Accounting Manual (SAAM) 30.40.80, states in part:

When suspected or known losses of inventorable assets occur, agencies should conduct a search for the missing property. The search should include transfers to other divisions or agencies, storage, scrapping, conversion to another asset, etc. If the missing property is not found: Follow the loss procedures in Section 20.30. Remove the lost or stolen property from the agency's inventory and accounting records where applicable (refer to Subsection 85.60.50). Maintain records for losses of inventorable assets in accordance with approved agency records retention schedules.

State Administrative and Accounting Manual (SAAM) 30.45.30, states in part:

Written physical inventory instructions must be documented and distributed to each person participating in the inventory process. The instructions should describe: How and where to record each item, What information to record, What to do when they have a question, What procedures to follow when they finish their assignments, What procedures to follow when equipment is located but not listed, The procedure by which the person counting the assets attests to the accuracy of the count, such as by signing his or her name at the bottom of each inventory page, or signing a cover page for a group of pages sorted by another method (batches, location, equipment type, etc.), and How to record assets not being used or in an obviously unserviceable condition.

State Administrative and Accounting Manual (SAAM) 30.45.40, states in part:

After the physical inventory count is completed, the agency inventory officer is to conduct the reconciliation process. When all differences have been identified and explained, the inventory is considered reconciled.

Washington Military Department Policy: Inventory, Financial Services Policy
Number 02-001-02, states in part:

4. POLICY: All employees of the Military Department will safeguard the state-owned assets as resources of the state. To safeguard the assets, the Military Department will conduct a physical inventory of assets every two years.

Schedule of Audit Findings and Responses

State of Washington Military Department

2. Washington Military Department's monitoring of Youth Academy purchase card use is not sufficient to prevent or detect misuse.

Background

In January 2009, the Department began operating the Washington Youth Academy in Bremerton. The Academy is a division of the Department and is a state-run program for 16-19 year olds who have dropped out of high school or are at risk of dropping out. The Department issued two purchase cards to the Academy for food and supply purchases.

During the six months in fiscal year 2009 after the Academy began operations, it purchased goods and services totaling \$717,471.46; approximately 30 percent of that amount – \$216,000 – was charged to the purchase cards. Purchase card activity during this time averaged \$36,000 per month.

Description of Condition

Department management established detailed policies and procedures to ensure the cards are controlled, safeguarded and managed in accordance with state regulations. We met with Department staff to discuss the approval and payment of purchase card expenditures at the Academy to determine if it was following Department policies and procedures.

Documentation

The Department does not have signed user agreements for designated card users to ensure they have been trained in the allowable use of the cards. User agreements are required by state regulations as evidence that card users understand and agree to policies.

The Youth Academy does not maintain transaction logs for all purchases as required by Department and State policies. Transaction logs document who was provided the card and for what purpose. It is also a place to document that the card was returned and to attach purchase receipts.

Approvals

Academy management stated it requests preapproval only for purchases that exceed \$3,300. Department policy requires preapproval for any single transaction over \$250.

There is no secondary review of purchases made by the Academy approving manager. The approving manager stated he makes approximately 20 percent of the total purchases with one of the assigned cards.

Reconciliation

The Youth Academy management does not require or maintain original receipts for each transaction, nor does it ensure timely and accurate reconciliation of purchase card statements as required by Department and state policies.

Cause of Condition

Management responsible for ensuring compliance by Academy staff with Department policy and state regulations failed to do so. Staff did not appear to be fully aware of purchasing policies, and were neither held to policy standards nor monitored for compliance.

Department management does not provide effective oversight of purchases

Effect of Condition

The policies and procedures required by State regulations and adopted by Department management are intended to ensure accountability for the use of purchase cards and prevent misuse. When those policies and procedures are circumvented, management has no assurance that improper use would be prevented or detected.

Without signed card user agreements, the Department may face difficulty holding employees accountable in the event of improper use. By not maintaining transaction logs, the Department cannot assign responsibility for purchase card activity.

We intended to test purchase activity to determine if all purchases were allowable and for legitimate Department purposes. However, when we reviewed four monthly billing statements selected for testing, we found approximately \$39,000 of the \$109,000 purchases made during those months were not supported with receipts. Without a receipt supporting each purchase, Department management cannot verify all purchases are allowable and detect improper activity timely, if at all.

A reconciliation of receipts to billing statements is not possible since all transactions do not have a supporting receipt.

Additionally, we found Youth Academy management was unaware that the pre-approval for purchases over \$250 required by policy was seldom obtained. Management indicated it received "four or five" over-limit requests per month. We found more than 20 such purchases occurred in a month.

Recommendation

We recommend the Department review purchasing department activities to ensure compliance with Department policies and state regulations.

Department's Response

We agree with this finding. We began seeing potential problems in this new division of the agency in late 2009 just as the audit was getting started. We began developing a more stringent approach to management of purchase card transitions but held off in

implementing them until the audit was complete in the event other problems were discovered that required additional attention.

Now that we have a full picture of the issue at hand, we are in the process of updating and revising the credit card policy and procedures to more closely align them with our current online system, we are also updating the language, clarifying roles and responsibilities and eliminating any redundancies. The Youth Academy business manager is on the work team charged with rewriting this document.

We obtained signed user agreements and counseled the cardholders on the proper uses of the card, why they must maintain a transaction log, the importance of timely reporting and reconciliation and the necessity to maintain original receipts for each transaction.

Once the new policy and procedures have been finalized, we will distribute the information to all relevant staff in the agency including credit card holders, credit card users and supervisors. We will also conduct group training session to ensure staff fully understands the new policy and procedures and ensure there is a common understanding of the requirements, and roles and responsibilities.

Auditor's Remarks

We appreciate the cooperation and assistance provided by the Department throughout the audit. We will follow up with the Department to review the status of its corrective action at a later date.

Applicable Laws and Regulations

SAAM Chapter 45 – Purchase Cards, states in part:

45.10.60.a Agency responsibilities

- Administration of their agency's purchasing card program.
- Developing agency specific policies and procedures in accordance with state policies.
- Educating cardholders, card custodians, and designated card users on use of the card, sales and use tax issues, and 1099 reportable merchants.

45.20.30 Transaction log

Agencies must utilize a purchase card transaction log to record each purchase made using the purchase card.

45.20.50 Reconciliation, documentation, and records retention

Responsibility for reconciliation of the card statement rests with the cardholder or card custodian. The cardholder or card custodian should reconcile purchases made during the billing cycle by matching the bank statement or online purchase card

transaction data to their purchase card transaction log and the documentation obtained from the merchant on purchases.

A pattern of missing documentation should result in the loss of purchase card privileges. Agencies are required to monitor and cancel the purchase card for card users who frequently do not provide appropriate purchase card supporting documentation.

Washington Military Department Financial Services Policy 02-003-02, states in part:

d. Card Custodian will:

(3) maintain the transaction log for all purchases

(4) maintain all original receipts for each transaction

(5) report to the Approving Manager any known or suspected inappropriate use of the Purchase Card

(6) report lost or stolen cards immediately

7. Limits

b. Single Transaction. The single transaction limit shall not exceed \$250 without prior approval from the Military Department Purchasing and inventory Office. Purchases shall not be deliberately split into smaller parts to circumvent this limit.

Washington Military Department Financial Services Procedure 02-003-02, states in part:

Transaction Log: The transaction log must be maintained by the Card Custodian and sent to the Military Department Purchasing and Inventory Office on the last business day of the month along with all transaction receipts and additional documentation if required.

Monthly Reconciliation: The Purchase Card Manager (or designee) will reconcile the monthly transaction log to the monthly billing statement. If discrepancies are found, the Purchase Card Manager will contact the Card Custodian for additional information.

Status of Prior Audit Findings

State of Washington Military Department

The status of findings contained in the prior years' audit reports of the Military Department is provided below:

1. The Military Department is not accurately calculating survivor death benefit compensations.

Report No. 1000335, dated December 22, 2008

Background

State law says that when a National Guard employee dies while performing noncombat duties, the Department is to make death benefit payments to his or her spouse or dependents. In 2007-2008 the Department paid benefits to four individuals. In the prior audit, we reviewed death benefit payments and found the Department had incorrectly calculated some of them. The total paid between July 1, 2005, and August 1, 2008, was approximately \$286,000. Of that, \$51,665 was an adjustment to correct a benefit calculation error occurring from July 1998 through June 2005.

Status

The Department's risk manager, who has experience in the calculation of death benefits, reviewed the calculations for all death benefits going back to the start of each claim. The Department also consulted with the Department of Labor and Industries Insurance Services staff that has the expertise to calculate benefit payments. They examined the risk manager's review and agreed with the recalculations.

The Department completed a detailed comparison between the recalculated death benefits and original benefits. As a result, the Department adjusted or is in the process of adjusting monthly benefits.

The Department is also in the process of drafting policy and procedures for processing death benefit claims and for maintaining the related records and files. These actions resolved the issues in the finding.

2. The Military Department's internal controls over fixed assets are not sufficient to safeguard public assets.

Report No. 1000335, dated December 22, 2008

Background

In fiscal year 2008, the Military Department had inventory valued at approximately \$11.5 million, consisting primarily of technology items, such as communications equipment, laptops and personal computers. Department policies and procedures

require all equipment with a purchase price of more than \$5,000 must be included in its inventory tracking system. In addition, items easily subject to misappropriation or loss, such as laptop computers and cameras, must be inventoried.

The Department is required to maintain an accurate and complete list of its fixed and small and attractive assets through use of the state's Capital Asset Management System (CAMS). When items are missing, lost or misappropriated, the Department is required to perform an adequate search and remove them from CAMS if it cannot locate them. The Department also is required to dispose of surplus assets in accordance with Department policy.

Status

This issue was not resolved and the finding is repeated. See Schedule of Audit Findings and Responses, Finding 1, "The Military Department has an incorrect interpretation of state regulations regarding counting, reconciliation and certification of its asset inventory."